Decision ______________________

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Pacific Terminals LLC for Authorization to Guarantee Its Parent's Debt and Related Obligations, to Encumber Its Public Utility Property, and to Treat the Cancellation of Its Outstanding Debt as Additional Members' Contribution, or Alternatively, to Incur Indebtedness Payable More than Twelve Months after the Date Incurred.	Application 03-07-051 (Filed July 31, 2003)

OPINION AUTHORIZING THE REFINANCING OF DEBT

I. Summary

This decision authorizes Pacific Terminals LLC (PT) to replace $167 million of short-term debt owed to PT's parent company with (1) $67 million of equity capital from the parent company, and (2) $100 million of secured debt owed to the parent company that will mature on July 26, 2007.[1]

II. Background

PT is a pipeline corporation as defined by Pub. Util. Code §§ 216(a), 227, and 228, and is subject to the Commission's jurisdiction pursuant to § 216(b). PT was formed for the specific purpose of owning and operating fuel oil pipeline and storage facilities (FOP&S facilities) acquired from Southern California

[1] The Commission has not assigned a utility identification number to PT (or to several other pipeline corporations). Hence, the caption for this proceeding does not contain a utility identification number pursuant to Rule 2.1(c).

Edison Company (SCE). Decision (D.) 03-07-031 authorized PT to purchase the FOP&S facilities for $158.2 million and to operate the facilities as a public utility.

PT is owned by Pacific Energy Group LLC (PEG).[2] On July 19, 2002, PEG entered into a credit agreement with Fleet National Bank and several other lenders (collectively "Fleet"). The Fleet Credit Agreement includes a $200 million revolving credit facility that matures on July 26, 2007.[3] PEG's obligations under the Fleet Credit Agreement are guaranteed by all of PEG's operating subsidiaries except PT and Pacific Pipeline System LLC (PPS). Like PT, PPS is a pipeline corporation subject to the Commission's jurisdiction. The guaranty provided by the other subsidiaries is secured by the subsidiaries' assets, with one *de minimis* exception.[4] PT and PPS did not provide a guaranty or security arrangement because neither had prior Commission authority to do so.

On July 31, 2003, PEG drew $149 million from the revolving credit facility and advanced such proceeds, plus $10 million of PEG's own money, to PT to fund PT's acquisition of SCE's FOP&S facilities. PT estimates that an additional $8 million will be drawn from the revolving credit facility to pay post-closing purchase price adjustments. In return for the funds provided by PEG, PT gave an unsecured note to PEG for $167 million that bears the same interest rate as the

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[2] PEG is owned by Pacific Energy Partners, L.P., a publicly traded limited partnership.

[3] The Fleet Credit Agreement is attached to Application (A.) 03-07-051 as Exhibit 4.

[4] PT represents that the guaranty provided by Pacific Marketing and Transportation, LLC is not secured by its property because the value of the property did not warrant the cost that would have been incurred to provide the security interest.

Fleet revolving credit facility. PT's note to PEG matures on July 30, 2004, which is less than 12 months from the date the note was issued.[5]

III. The Application

In its application, as amended,[6] PT requests authority to guarantee $167 million of debt that was incurred by PT's parent, PEG, so that PT could purchase the FOP&S facilities from SCE and to secure such guarantee with PT's operating assets. Upon such approval, PT's outstanding short-term debt owed to PEG would be cancelled and treated as additional equity.[7]

PT offers two reasons why the Commission should authorize the guaranty and encumbrance. First, it provides PT with an orderly means of refinancing $167 million of debt that matures in July 2004. Second, the debt that PT would indirectly assume under the Fleet Credit Agreement has terms and conditions that are better than PT could obtain on its own.

If the Commission denies PT's request to enter into the proposed guaranty and security arrangements, then PT requests authority to replace $167 million short-term debt owed to PEG with (1) $67 million of equity from PEG,[8] and (2) $100 million of debt owed to PEG that would mature on July 26, 2007. PT

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[5] Pub. Util. Code § 823(b) authorizes public utilities to issue debt that matures in less than 12 months without the consent of the Commission so long as such debt is used for proper purposes and does not violate any law.

[6] PT filed A.03-07-051 on July 31, 2003, and an amendment to A.03.07-051 on November 10, 2003. PT also filed a supplement to A.03-07-051 on August 29, 2003.

[7] Like PT, PPS filed an application (A.03-07-052) to guarantee debt, to encumber public utility property, and to treat the cancellation of debt as additional equity, or alternatively, if such request was denied, to incur long-term debt. PPS's alternate request was granted by the Commission in D.03-10-078.

[8] In other words, accounting entries would be made to PT's books to transform $67 million of short-term debt owed to PEG into $67 of equity capital from PEG.

would secure the $100 million of new debt by granting mortgage and security interests in certain of its properties to PEG. The terms and conditions of the new debt would be substantially the same as those in the revolving loan facility under the Fleet Credit Agreement, modified to reflect PT's proportionate share of any interest rate hedge agreement entered into by PEG. The interest rate on the new debt would equal the London Interbank Offering Rate (LIBOR)[9] plus 275 basis points through March 31, 2004, and LIBOR plus 225 basis points after March 31, 2004. PEG would pledge its note from PT to Fleet.

PT states that it has the financial capacity to pay interest on $100 million of debt while continuing to provide safe and reliable service to the public. To demonstrate this point, PT submitted a forecast of PT's pro forma results of operations, assuming a capital structure of $100 million of debt and $67 million of equity.[10] The forecast was derived from the forecast prepared in conjunction with the public offering of Pacific Energy Partners, L.P. in July 2002 that was included in Form S-1/A filed with the Securities and Exchange Commission (SEC) on July 19, 2002.[11] The pro forma financial forecast shows that revenues from the operation of the FOP&S facilities will provide sufficient cash to fund PT's day-to-day operations, maintenance and repairs, interest on debt, and

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9 There are several LIBOR rates (e.g., 1-month rate, 3-month rate, and 12-month rate). PT may select any LIBOR rate between one and twelve months' duration.

10 See Amendment to A.03-07-051, Exhibit 1, which was verified in accordance with Rule 2.4 by Irvin Toole, Jr., the President and CEO of PT.

11 PT represents that it cannot provide meaningful historical financial statements for the FOP&S facilities because of the way SCE accounted for facilities. For example, SCE did not allocate some major operating expenses to the FOP&S assets, such as insurance and power costs.

distributions to equity members. PT represents that its actual results of operations to date are consistent with the forecast that was filed with the SEC.

Notice of A.03-07-051 appeared in the Commission's Daily Calendar on August 6, 2003. Notice of PT's amendment to A.03-07-051 appeared in the Daily Calendar on November 10, 2003. There were no protests or other responses to either the application or the amendment.

IV. Discussion

The primary issues in this proceeding are whether PT should be authorized to refinance $167 million of short-term debt and, if so, how PT should refinance the debt. Resolution of these issues is subject to Pub. Util. Code § 816 et seq., and § 851, which state, in relevant part, as follows:

> **Section 816:** The power of public utilities to issue [debt and equity] is a special privilege, the right of supervision, regulation, restriction, and control of which is vested in the State, and such power shall be exercised as provided by law under such rules as the commission prescribes.
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> **Section 817(d):** A public utility may issue [debt and equity] . . . for . . . the following purposes and no others . . . (d) For the discharge or lawful refunding of its obligations.
>
> **Section 818:** No public utility may issue [debt or equity] . . . unless . . . it shall first have secured from the commission an order authorizing the issue, stating the amount thereof and the purposes to which the issue or the proceeds thereof are to be applied, and that, in the opinion of the commission, the money, property, or labor to be procured or paid for by the issue is reasonably required for the purposes specified in the order, and that . . . such purposes are not, in whole or in part, reasonably chargeable to operating expenses or to income.
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> **Section 823(d):** No note payable at a period of not more than 12 months after the date of issuance of such note shall,

> in whole or in part, be refunded by [debt or equity] . . . without the consent of the commission.
>
> **Section 830:** No public utility shall assume any obligation or liability as guarantor, endorser, surety . . . without having first secured from the commission an order authorizing it so to do.
>
> **Section 851:** No public utility . . . shall . . . mortgage. . . any . . . of its . . . property necessary or useful in the performance of its duties to the public . . . without first having secured from the commission an order authorizing it so to do.

PT's balance sheet shows that PT does not have sufficient liquid assets to retire $167 million of debt.[12] Accordingly, we find that PT has a need to refinance $167 million of short-term debt that matures on July 30, 2004. We also find that the large size of the refinancing ($167 million) in relation to PT's projected annual revenues ($35.8 million) and pre-tax income ($13.4 million)[13] makes it impractical for PT to charge the cost of the refinancing to operating expenses or income.

PT proposes two alternatives for refinancing $167 million of short-term debt that PT owes to its parent company. PT's preferred alternative is for the parent company to cancel the debt and for PT to treat the cancellation as $167 million in new equity. In return, PT would guarantee $167 million of debt already issued by the parent company and pledge its assets as collateral for the parent's debt. We presume that PT would also be responsible, either directly or indirectly, for paying the principal and interest on the parent's debt.

PT's preferred alternative amounts to off-balance-sheet financing. If we adopted this approach, PT's balance sheet would present the rosy but deceptive

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[12] PT's pro forma balance sheet dated August 1, 2003, shows total current assets of $1.264 million. (A.03-07-051, Exhibit 3.)

[13] Amendment to A.03-07-051, Exhibit 1.

picture of $167 million in equity and little or no debt, even though PT would be liable for $167 million of its parent's debt and be *de facto* responsible for paying this debt. We conclude that it is not in the public interest to authorize such financial arrangements, and we decline to adopt this approach.

The second alternative is to replace $167 million of short-term debt that PT owes to its parent with (1) $67 million of equity capital from the parent, and (2) $100 million of new debt owed to the parent that would mature July 26, 2007. The new debt would be secured by granting mortgage and security interests in certain of PT's properties. The terms and conditions of the new debt would be substantially the same as the revolving loan facility in the Fleet Credit Agreement, modified to reflect PT's proportionate share of any interest rate hedge agreement entered into by the parent. PT's financial projections indicate that it has sufficient cash flow to service the new debt while continuing to fund day-to-day operations, maintenance and repairs, and distributions to equity members. We find this alternative to be straightforward and reasonable, and we will approve it pursuant to Pub. Util. Code § 816 et seq., and § 851.

V. Exemption from the Competitive Bidding Rule

Resolution F-616, issued on October 1, 1986, requires utilities to issue debt using competitive bids. The purpose of this requirement, known as the Competitive Bidding Rule, is to reduce the cost of debt issued by utilities. Resolution F-616 also exempted several types of debt from the Competitive Bidding Rule. The exempted debt includes securities privately placed with specific lenders, bank term loans, variable-interest debt, and debt issued by companies with bond ratings that are lower than A. The debt authorized by today's decision is variable-interest debt that falls within the stated exemptions.[14]

VI. Public Utilities Code § 1904(b)

Whenever the Commission authorizes a utility to issue debt, the Commission must collect a fee in accordance with § 1904(b), which states:

> For a certificate authorizing an issue of bonds, notes, or other evidences of indebtedness, two dollars ($2) for each one thousand dollars ($1,000) of the face value of the authorized issue or fraction thereof up to one million dollars ($1,000,000), one dollar ($1) for each one thousand dollars ($1,000) over one million dollars ($1,000,000) and up to ten million dollars ($10,000,000), and fifty cents ($0.50) for each one thousand dollars ($1,000) over ten million dollars ($10,000,000), with a minimum fee in any case of fifty dollars ($50). No fee need be paid on such portion of any such issue as may be used to guarantee, take over, refund, discharge, or retire any stock, bond, note or other evidence of indebtedness on which a fee has theretofore been paid to the commission. If the commission modified the amount of the issue requested in any case and the applicant thereupon elects not to avail itself of the commission's authorization, no fee shall be paid, and if such fee is paid prior to the issuance of such certificate by the commission, such fee shall be returned.

The $100 million of debt authorized by today's decision is subject to § 1904(b).[15] Therefore, PT shall remit $56,000 to the Commission's Fiscal Office no later than 60 days from the effective date of today's decision.[16]

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[14] PT intimates that the debt authorized by today's decision is exempt from the Competitive Bidding Rules because PT's debt is not rated and the debt of its parent is rated lower than A.

[15] Section 1904.1 is applicable to the issuance of stock and does not expressly address the contribution of equity capital by a parent entity. Today's decision does not

Footnote continued on next page.

VII. General Order 24-B

General Order (GO) 24-B requires utilities to submit a monthly report to the Commission that contains, among other things, the following information: (1) the amount of debt issued by the utility during the previous month; (2) the total amount of debt outstanding at the end of the prior month; (3) the purposes for which the utility expended the proceeds realized from issuance of debt during the prior month; and (4) a monthly statement of the separate bank account that the utility is required to maintain for all receipts and disbursements of money obtained from the issuance of debt.

PT requests authority to report quarterly the information required by GO 24-B in order to reduce the administrative cost of complying with the General Order.[17] PT's request is reasonable, and we hereby grant it.

VIII. Categorization and Need for Hearings

In Resolution (Res.) ALJ 176-3117 dated August 21, 2003, the Commission preliminarily categorized A.03-07-051 as ratesetting, and preliminarily determined that hearings were not necessary. Given the record of this proceeding, we affirm the preliminary determinations in Res. ALJ 176-3117.

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constitute precedent on whether § 1904.1 applies to equity contributions from a parent entity.

[16] \$56,000 = (\$2 x 1,000,000 / 1,000) + (\$1 x \$9,000,000 / 1,000) + (\$0.50 x 90,000,000 / 1,000) = \$2,000 + \$9,000 + \$45,000.

[17] The Commission routinely grants requests similar to PT's. See, e.g., D.03-10-078, D.01-02-011, and D.00-12-064.

IX. Waiver of Comment Period

This is an uncontested matter in which the decision grants the relief requested. Accordingly, pursuant to Pub. Util. Code § 311(g)(2), the otherwise applicable 30-day period for public review and comment is waived.

X. Assignment of Proceeding

The assigned Commissioner for this proceeding is Susan P. Kennedy. The assigned Administrative Law Judge is Timothy Kenney.

Findings of Fact

1. PT has a need to refinance $167 million of short-term debt that it owes to its parent company, PEG. The large size of the refinancing in relation to PT's annual revenues and pre-tax income makes it impractical for PT to charge the cost of the refinancing to operating expenses or income at this time.

2. In A.03-07-051, PT requests, among other things, authority to replace $167 million of short-term debt owed to PEG with (i) $100 million of secured, variable-rate debt owed to PEG that would mature on July 26, 2007, and (ii) $67 million of equity from PEG. The $100 million of new debt would have terms and conditions that are substantially the same as those in the revolving loan facility contained in the Credit Agreement between PEG and Fleet, modified to reflect PT's proportionate share of any interest rate hedge agreement entered into by PEG. The new debt would be secured by granting mortgage and security interests in PT's public utility property.

3. PT provided information that indicates PT has sufficient cash flow to (i) service the debt identified in Finding of Fact No. 1, and (ii) fund day-to-day operations, maintenance and repairs, and distributions to equity members.

Conclusions of Law

1. PT should be authorized pursuant to Pub. Util. Code §§ 816 et seq., and § 851 to replace $167 million of short-term debt owed to PEG with (i) $100 million of secured debt owed to PEG that would mature on July 26, 2007, and (ii) $67 million of equity from PEG. The new debt should have terms and conditions that are substantially the same as those set forth in A.03-07-051.

2. The variable-rate debt authorized by today's decision is exempt from the Competitive Bidding Rule set forth in Resolution F-616.

3. PT is required by Pub. Util. Code Section 1904(b) to remit a fee of $56,000 for the debt authorized by today's decision.

4. Today's decision should not be construed as precedent on whether § 1904.1 applies to contributions of equity capital from a parent entity.

5. The debt authorized by today's decision is subject to GO 24-B.

6. PT should be authorized to report quarterly the information required by GO 24-B to reduce the administrative cost of complying with the General Order.

O R D E R

IT IS ORDERED that:

1. Pacific Terminals LLC (PT) is authorized pursuant to Pub. Util. Code § 816 et seq., to incur indebtedness in the amount of $100 million, with a maturity date of July 26, 2007, on terms and conditions that are substantively consistent with those set forth in Application 03-07-051, as amended.

2. PT is authorized pursuant to Pub. Util. Code §§ 816 et seq., and 851 to encumber its property by granting mortgage and security interests therein in conjunction with the debt authorized by the preceding Ordering Paragraph. The amount of such encumbrance shall not exceed $100 million.

3. PT is authorized pursuant to Pub. Util. Code § 816 et seq., to covert $67 million of short-term debt owed to its parent, Pacific Energy Group LLC (PEG), into equity capital provided by PEG.

4. PT shall use the debt and equity authorized by this Order for the sole purpose of retiring $167 million of existing short-term debt owed to PEG.

5. Pursuant to Pub. Util. Code § 1904(b), PT shall remit a fee of $56,000 to the Commission's Fiscal Office no later than 60 days from the effective date of this Order. The authority granted by this Order shall (i) not commence until PT remits the required fee, and (ii) terminate if PT does not remit the required fee within the specified timeframe.

6. PT may report quarterly the information required by General Order 24-B.

7. Application 03-07-051 is granted as set forth above.

8. This proceeding is closed.

This Order is effective today.

Dated ____________________________, at San Francisco, California.